

ORIGINAL



0000134806

Laura E. Sanchez
NATURAL RESOURCES
DEFENSE COUNCIL
PO Box 65623
Albuquerque, NM 87193
(505) 352-7408
lsanchez@nrdc.org

RECEIVED
AZ CORP COMMISSION
DOCKET CONTROL

2012 MAR 1 PM 2 51

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

Arizona Corporation Commission

DOCKETED

GARY PIERCE – Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

MAR - 1 2012

DOCKETED BY

IN THE MATTER OF THE APPLICATION OF
ARIZONA PUBLIC SERVICE COMPANY FOR A
HEARING TO DETERMINE THE FAIR VALUE OF
THE UTILITY PROPERTY OF THE COMPANY
FOR RATEMAKING PURPOSES, TO FIX A JUST
AND REASONABLE RATE OF RETURN
THEREON, TO APPROVE RATE SCHEDULES
DESIGNED TO DEVELOP SUCH RETURN.

Docket No. E-01345A-11-0224

NRDC's OPENING BRIEF

Natural Resources Defense Council ("NRDC") hereby submits this Opening Brief on matters
raised in the recent Arizona Public Service Company ("APS") rate hearing.

Table of Contents

I.	INTRODUCTION AND SUMMARY.....	2
II.	THE ORIGINAL APS PROPOSAL FOR FULL DECOUPLING WAS MADE AT THE COMMISSION'S INVITATION AND WAS FULLY CONSISTENT WITH COMMISSION PRECEDENT.....	3
III.	SECTION IX OF THE PROPOSED SETTLEMENT AGREEMENT IS FLATLY INCONSISTENT WITH RECENT COMMISSION PRECEDENT AND INCOMPATIBLE WITH THE PUBLIC INTEREST IN ENHANCED ENERGY EFFICIENCY AND LOWER ELECTRICITY BILLS.....	4
IV.	CONCLUSION.....	8

1 **I. INTRODUCTION AND SUMMARY**

2 Only weeks after its decision in the Southwest Gas rate case, the Commission faces a virtually
3 identical choice on whether to decouple a utility's financial health from increases in its retail energy
4 sales. This time opponents of full decoupling have simply repackaged positions identical to those
5 rejected by the Commission earlier this year in item IX of a proposed "Settlement Agreement," which
6 NRDC did not join. The Commission should reject this transparent attempt to disregard conclusions
7 reached in both the Southwest Gas case and in a Final Policy Statement adopted only a year earlier
8 after extensive workshops and deliberations.
9

10 In this proceeding, NRDC and SWEEP are urging the Commission to adopt the full
11 decoupling mechanism that APS originally proposed. APS, Staff and others are contending that the
12 Commission should accept a clearly inferior "compromise" in the form of a lost fixed-cost recovery
13 mechanism virtually identical to the one it rejected in the Southwest Gas case (paired, ironically and
14 implausibly, with the straight fixed-cost rate design option that RUCO offered unsuccessfully in the
15 same case). The only relevant difference between the two proceedings is that in the Southwest Gas
16 case a proposed settlement (which NRDC and SWEEP joined) invited the Commission to choose
17 between full decoupling and lost fixed-cost recovery, whereas in this case the proposed settlement
18 attempts to prevent the Commission from making the same choice, by including only the inferior
19 alternative in the body of the Agreement. The Commission should resolve this issue in the only way
20 that is consistent with its Southwest Gas precedent: substitute full decoupling (in the form of the
21 original APS proposal) for the hybrid form of lost fixed-cost recovery and straight fixed-variable rate
22 design proposed in section IX of the Settlement Agreement.
23
24
25
26
27
28

1 **II. THE ORIGINAL APS PROPOSAL FOR FULL DECOUPLING WAS MADE AT THE**
2 **COMMISSION'S INVITATION AND WAS FULLY CONSISTENT WITH**
3 **COMMISSION PRECEDENT.**

4 NRDC witness Cavanagh's direct testimony urged the Commission to approve the Arizona
5 Public Service Company's (APS) proposal for an Efficiency and Infrastructure Account ("EIA"),
6 which represented a straightforward per-customer decoupling mechanism of the very type endorsed
7 and solicited in the Final Policy Statement adopted unanimously by the Commission less than a year
8 earlier.¹ After the filing of this testimony, the Commission approved (on December 13, 2011) a very
9 similar per-customer decoupling mechanism for the Southwest Gas Company, based on a settlement
10 proposal that left the Commission a clear choice between full decoupling and a lost revenue recovery
11 mechanism. The Commission's decision in favor of full decoupling included a thorough review of
12 policy and legal issues, with numerous references to the Final Policy Statement.
13

14
15 That same Policy Statement is cited repeatedly in witness Cavanagh's direct testimony as the
16 primary basis for NRDC's support of APS's revenue decoupling proposal. Although some parties are
17 using this proceeding to voice long-standing philosophical disagreements with full decoupling, none
18 have challenged the consistency of APS's initial proposal with either the Commission's Policy
19 Statement or its decision in the Southwest Gas case. Although it supports the settlement, APS itself
20 has not disavowed any element of its initial proposal, and its witness's Responsive Testimony states
21 that "I am not going to tell the Commission that Full Decoupling would not remove the current
22 financial disincentive to the Company presented by energy efficiency and DG."² APS also
23 acknowledges in its Response Testimony that "[u]nder terms of the Settlement, the Commission is
24
25
26

27
28 ¹ Arizona Corporation Commission, Final Policy Statement Regarding Utility Disincentives to Energy Efficiency and
Decoupled Rate Structures, Docket Nos. E-00000J-08-0314 and G-00000C-08-0314 (December 29, 2010) ("Final Policy
Statement").

1 not bound to make any particular resolution of the unrecovered fixed cost problem and could adopt
2 Full Decoupling.”³ That is exactly what the Commission should do.

3
4 **III. SECTION IX OF THE PROPOSED SETTLEMENT AGREEMENT IS FLATLY**
5 **INCONSISTENT WITH RECENT COMMISSION PRECEDENT AND**
6 **INCOMPATIBLE WITH THE PUBLIC INTEREST IN ENHANCED ENERGY**
7 **EFFICIENCY AND LOWER ELECTRICITY BILLS.**
8

9 The proposed Settlement Agreement essentially substitutes Staff’s proposal for lost fixed-cost
10 recovery (LFCR) for the APS decoupling proposal, while adding RUCO’s preferred straight fixed
11 variable rate design as an “opt out” alternative. Other parties refer to this misbegotten combination
12 as a “hard bargained agreement” and a “broad consensus” that the Commission should accept in the
13 spirit of compromise.⁴
14

15 But parties to a proposed settlement, regardless of their number, cannot bargain away
16 Commission precedent and policy. And the Commission itself has on two recent occasions rejected
17 exactly what Section IX of the proposed settlement offers. The first such occasion was the Final
18 Policy Statement, adopted on December 29, 2010, which stated a clear preference for “full
19 decoupling” compared to “lost margin recovery mechanisms” and straight fixed-variable rate design.⁵
20
21

22 ² Responsive Settlement Testimony of Jeffery B. Guldner on behalf of Arizona Public Service Company (Jan. 25, 2012),
p. 2:22.

23 ³ Id. at p. 4: 6-8 (January 25, 2012).

24 ⁴ See, e.g., Rebuttal Testimony of Nancy Brockway on behalf of AARP, p. 3:8 (January 25, 2012); Responsive Settlement
Testimony of Jeffery B. Guldner on behalf of Arizona Public Service Co. (January 25, 2012), p. 4:12.

25 ⁵ See Final Policy Statement, note 1 above, at pp. 28-29: “Fixed cost/variable pricing would result in larger customer
charges, which impact low-income customers, and reduced variable charges, which discourages efficient energy use.
26 Lost margin recovery mechanisms allow for recovery of margins attributable to decreased sales from energy efficiency
programs; however, this mechanism may be subject to prolonged litigation, and would not allow for other beneficial
27 actions on rate design or contribute to improved costs of capital . . . [F]ull decoupling is preferable as it enhances utility
and customer billing stability, is administratively more manageable and would allow for rate relief during extreme
28 weather events.” For a similar comparison favoring full decoupling over “alternative mechanisms” such as those
proposed in the Settlement Agreement, see Id., p. 4, concluding that “properly structured, decoupling offers significant
advantages over alternative mechanisms.”

1 The second was the January 2012 Southwest Gas decision.⁶ In proposing to substitute decoupling for
2 the lost fixed-cost recovery provision in the proposed settlement, NRDC and SWEEP are framing for
3 the Commission the same choice that it faced in the Southwest Gas case. There, a stipulation joined
4 by Staff, NRDC and SWEEP asked the Commission to select either a lost fixed-cost recovery
5 mechanism (Alternative A, favored by Staff) or full revenue decoupling (Alternative B, favored by
6 NRDC and SWEEP). The Commission chose Alternative B, reaffirming the preference stated in its
7 Final Policy Statement:
8

9 [A] partial decoupling mechanism such as is included in Alternative A could create
10 conflicting incentives for the Company by, on the one hand, imposing significant energy
11 efficiency goals that must be achieved while, on the other hand, leaving in place a structure
12 that would concurrently provide an incentive for SWG to sell higher volumes of gas in order
13 to improve its bottom line, thereby undermining the Policy Statement's goal of encouraging
14 conservation. Another concern raised by Alternative A is the nature of the annual proceedings
15 that would be required to review the performance of the LFCR mechanism, and the likelihood
16 that those proceedings would be extremely adversarial as parties were forced to litigate on a
17 yearly basis whether SWG had achieved the required energy efficiency goals. Further, as Mr.
18 Cavanagh pointed out, adoption of Alternative A may cause SWG to pursue energy efficiency
19 programs that look good on paper but deliver much less in actual savings.⁷

20 In its lost fixed-cost recovery provision, the proposed settlement in this proceeding is really just
21 resurrecting Alternative A from the Southwest Gas case, this time in an attempt to displace outright
22 another clearly preferable full decoupling mechanism designed in full accord with the Commission's
23 Policy Statement.

24 Moreover, the proposed LFCR affects only "a portion of distribution and transmission costs,"
25 and entirely omits fixed costs of generation.⁸ In NRDC witness Cavanagh's words, "[t]his means that
26 even for savings potentially eligible for fixed cost recovery under the Settlement Agreement, APS
27 would be better off financially if it gave up the savings and received instead equivalent increases in
28

⁶ Decision No. 72723, Docket No. G-01551A-10-0458 (January 6, 2012).

⁷Id., pp. 39-40.

⁸ Proposed Settlement Agreement, p. 10, section 9.3.

1 retail sales.”⁹ Worse still, in the words of the Final Policy Statement, all other electricity savings
2 would automatically “impact recovery of fixed costs and investment returns,” even as “sales growth .
3 . . offers the opportunity to recover fixed costs and earn profit;” this is precisely the dilemma that the
4 Commission aimed to eliminate in its Policy Statement and its subsequent Southwest Gas decision.¹⁰
5 Moreover, no party contests NRDC witness Cavanagh’s observation that, here as in the Southwest
6 Gas case, “the LFCR represents an automatic rate increase, whereas decoupling can either raise or
7 reduce rates.”¹¹

9 The proposed settlement allows customers to “opt-out” of contributing to lost revenue
10 recovery, but only by incurring higher fixed charges and reductions in the rewards that they would
11 otherwise receive in their APS bills for saving electricity. The Commission’s Policy Statement
12 considered this rate design option and noted that it would adversely affect low-income customers and
13 discourage efficient energy use.¹² The Commission went on to reject a virtually identical proposal
14 from RUCO in the Southwest Gas case, on the ground that it would not “be consistent with the stated
15 goals of the Policy Statement.”¹³ Section 9.7 of the Proposed Settlement proposes the same kind of
16 rate design change for large customers, as an unconvincing basis for exempting them from the LCFR
17 mechanism and its automatic rate increases. Again, in the Commission’s own words, this move
18 toward “fixed cost/variable pricing” and larger customer charges would yield “reduced variable
19 charges, which discourages efficient energy use.”¹⁴ As AARP’s witness conceded before she
20
21
22
23
24

25 ⁹ Testimony of Ralph Cavanagh for NRDC in Partial Opposition to the Proposed Settlement Agreement (January 17,
26 2012), p. 8:6-10.

27 ¹⁰ See Final Policy Statement, note 1 above, p. 2 and Decision No. 72723, note 6 above.

28 ¹¹ Testimony of Ralph Cavanagh for NRDC in Partial Opposition to the Proposed Settlement Agreement (January 17,
2012), p. 7: 12-14.

¹² Final Policy Statement, note 1 above, p. 28.

¹³ Decision No. 72723, note 6 above, pp. 40-41.

¹⁴ Final Policy Statement, note 1 above, p. 28.

1 endorsed the proposed settlement, reducing variable charges and raising fixed charges means that
2 “the cost and effort of making usage more efficient would be rewarded with lower bill reductions.”¹⁵

3 The settlement parties’ only effort to distinguish the Southwest Gas case involves wholly
4 implausible contentions that natural gas and electricity are somehow different as regards the need for
5 revenue decoupling in order to remove barriers to energy efficiency, “because an electric utility has
6 no need to build load on its own” and “there is no need to adopt a mechanism (revenue decoupling)
7 guaranteed to take back the per customer growth from the electric utility as a punitive measure.”¹⁶

9 Putting aside the puzzling characterization of revenue decoupling as “punitive,” the short
10 answer to this novel contention is that nothing in the Commission’s Policy Statement supports any
11 such distinction between gas and electric utilities. In fact the opposite conclusion emerges from the
12 economic evidence cited in the Policy Statement and the record of this proceeding: the case for full
13 decoupling is even stronger for electric utilities. As NRDC witness Cavanagh pointed out in his
14 testimony at the Commission’s January 31 hearing, electric utilities experience significantly stronger
15 linkages between financial health and commodity sales than their natural gas counterparts, because
16 they recover much greater amounts of fixed costs in variable charges.¹⁷ In addition, the economic
17 benefits of the energy efficiency that revenue decoupling unleashes are substantially greater for
18 electric utilities and their customers. Specifically, from the perspective of APS customers, “benefits
19 from the proposed [full decoupling] mechanism are illustrated by the specific reference in the
20 Commission’s policy statement to opportunities for ‘direct bill savings to [APS] ratepayers on the
21 order of \$4.6 billion between 2011 and 2030,’ which ‘were principally driven by utility plant
22
23
24
25
26

27 ¹⁵ Direct Testimony of Nancy Brockway on behalf of AARP, p. 23:11-12.

28 ¹⁶ Responsive Testimony of Howard Solganick for the Utilities Division (January 25, 2012), p. 8:11-15.

¹⁷ Transcript at ____.

1 deferrals and by reductions in utility fuel and purchased power budgets' associated with the enhanced
2 energy efficiency efforts required to comply with the Commission's Energy Efficiency Standard."¹⁸
3

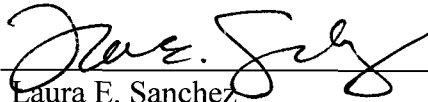
4 **IV. CONCLUSION**
5

6 NRDC recommends that the Commission resolve the decoupling issue just as it did in its
7 January 2012 Southwest Gas decision, by rejecting section IX of the Settlement agreement and
8 substituting the full decoupling proposal originally offered by APS in this proceeding, in order to
9 realize the Commission's energy efficiency goals, provide reasonable financial stability for this
10 utility, and ensure customer benefits through steadily increasing and highly cost-effective energy
11 savings.
12

13 RESPECTFULLY SUBMITTED this 29th day of February, 2012.

14 NATURAL RESOURCES DEFENSE COUNCIL

15 By



16 Laura E. Sanchez

17 PO Box 65623, Albuquerque, NM 87193

18 (505) 352-7408 | lsanchez@nrdc.org

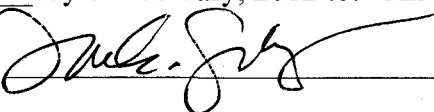
Attorney for NRDC

19 ORIGINAL and 13 COPIES of the foregoing
20 filed this 29th day of February, 2012 to:

21 Docketing Supervisor
22 Docket Control
23 Arizona Corporation Commission
1200 W. Washington
Phoenix, AZ 85007

24 COPIES of the foregoing electronically mailed this
25 29th day of February, 2012 to: All Parties of Record

26 By:



27
28 ¹⁸ Direct Testimony of Ralph Cavanagh for NRDC (November 17, 2011), pp. 4-5.